

No. 17361✓

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**United States**  
**COURT OF APPEALS**  
**for the Ninth Circuit**

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STANDARD LUMBER CO., formerly  
Pilot Rock Lumber Co.,

*Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE,  
*Respondent.*

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**PETITIONER'S BRIEF**

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*Appeal from the Tax Court of the United States.*

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**STATEMENT OF PLEADINGS AND**  
**BASIS OF JURISDICTION**

This is an appeal from the decision of the Tax Court of the United States which affirmed the determination of the Commissioner of Internal Revenue that corporation income tax deficiencies existed as to the petitioner for the taxable years 1954 and 1955. Appellate jurisdiction and venue are granted this Court by 26 U.S.C.A. §§ 7482(a) and 7482(b)1. The Tax Court had jurisdiction by virtue of 26 U.S.C.A. § 7442.

## STATEMENT OF THE CASE

Petitioner, Standard Lumber Co., formerly Pilot Rock Lumber Co., is a dissolved and liquidated corporation which prior to its dissolution was incorporated under the laws of the state of Oregon, having its principal office at Pilot Rock, Oregon.

The controversy involves the proper determination of petitioner's liability for Federal Income Taxes for the taxable years 1954 and 1955. This in turn depends upon whether or not the petitioner and Oregon Fibre Products, Inc., an Oregon corporation (hereinafter referred to as "Oregon Fibre") were entitled to file a consolidated income tax return for the calendar year 1954 under the provisions of Section 1504(a)(2) of the Internal Revenue Code of 1954, and more specifically, whether or not petitioner at all times during the calendar year 1954 owned stock of Oregon Fibre possessing at least 80% of the voting powers.

At all times during the calendar year 1954 there were issued and outstanding no more than 120,000 shares of the common stock of Oregon Fibre. Petitioner owned 74,000 of such shares and 30,000 of such shares were held by voting trustees under a 20 year voting trust agreement dated November 3, 1952. In 1953 the Oregon Legislature passed a law, to be effective December 31, 1953, that a voting trust agreement could be created for a period not to exceed ten years (ORS 57.175). On January 1, 1955, by mutual agreement, the voting trust agreement dated November 3, 1952, was terminated.



Petitioner took the position that the 30,000 shares subject to the voting trust were divested of voting power by the passage of ORS 57.175 since a "pall of invalidity" was thereby placed over said trust and that neither the trustees nor equitable owners thereof had the right to vote said shares pending a judicial determination of the effect of ORS 57.175 on the validity of said voting trust. Therefore, petitioner, relying on its ownership of 74,000 of the remaining 90,000 shares of Oregon Fibre or 82% thereof, filed a consolidated return with Oregon Fibre for the calendar year 1954.

The Commissioner of Internal Revenue took the position that the 30,000 shares subject to said voting trust were shares with voting power and that, therefore, peittioner did not own at least 80% of the voting power of the Oregon Fibre stock and was thus not entitled to file a consolidated return with Oregon Fibre for the calendar year 1954. Because of this determination, the Commissioner recomputed petitioner's tax liability for the calendar years 1954 and 1955 and determined income tax deficiencies against petitioner as follows:

1954 .....	\$255,939.96
1955 .....	180,397.47

The opinion of the Tax Court of the United States affirmed the findings of the Commissioner of Internal Revenue that petitioner was not entitled to file a consolidated return for the calendar year 1954, and held that ORS 57.175 worked no suspension of the voting rights of the stock held in trust and that petitioner did not own stock of Oregon Fibre possessing at least 80% of the voting power in 1954 so as to entitle petitioner

and Oregon Fibre to file a consolidated return for that year. Thereafter, the Tax Court entered its decision under Rule 50 determining deficiencies in income tax due from the petitioner for the taxable years 1954 and 1955 in the amounts of \$208,092.16 and \$180,397.47, respectively.

### **SPECIFICATIONS OF ERRORS**

Petitioner contends that the Tax Court of the United States erred in the following particulars:

1. In finding and concluding that petitioner was not entitled to file a consolidated return with Oregon Fibre Products, Inc., an Oregon corporation, for the calendar year 1954, and therefore, in holding that there were deficiencies due from petitioner for the taxable years 1954 and 1955. This ultimate finding and conclusion of the Tax Court is based upon the subsidiary erroneous findings and conclusions specified in paragraphs 2 and 3 below.

2. In finding and concluding that the passage of § 57.175 of the Oregon Revised Statutes which became effective on December 31, 1953, did not result in a suspension of the voting power of 30,000 shares of Oregon Fibre Products, Inc. common stock held under a certain voting trust agreement created November 3, 1952, and terminated by mutual agreement on January 1, 1955.

3. In finding and concluding that § 57.175 of the Oregon Revised Statutes limiting the duration of voting trusts to ten years does not apply to pre-existing voting trusts so as to render them invalid if created for a period in excess of the statutory limit.



## SUMMARY OF ARGUMENT

Unlike the consolidated return arguments considered in prior reported cases, § 1504(a) of Internal Revenue Code of 1954 here involved, requires only that petitioner owned during 1954 Oregon Fibre Products, Inc. stock possessing 80% of the voting power,—not 80% of the voting stock. Where voting rights are suspended on voting stock, it is possible to own stock possessing 80% of the voting power without owning 80% of the voting stock. The voting rights on the 30,000 shares of Oregon Fibre Products, Inc., held under the Nov. 3, 1952 voting trust agreement were suspended during 1954, which suspension resulted in the fact that the 74,000 shares owned by petitioner possessed 80% of the voting power which could be marshalled at any stockholders' meeting held during 1954, the year in question. Such suspension of voting rights of the 30,000 shares was caused by the impact of the Oregon Business Corporation Act effective December 31, 1953 upon the voting trust. This Act limited voting trusts to a duration not in excess of ten years, while the November 3, 1952 voting trust had a duration of 20 years and was thus rendered invalid by the passage of this Act.

## ARGUMENT

The opinion of the Tax Court recognizes the fact that the subject twenty year voting trust agreement covering 30,000 shares of common stock of Oregon Fibre Products, Inc. was invalidated by Oregon Revised Stat-

utes § 57.175 authorizing voting trust agreements for periods not to exceed ten years, *if* Oregon Revised Statutes § 57.175 applies to voting trust agreements already in existence on December 31, 1953 when the section became effective as part of the new Oregon Corporation Law. However, the Tax Court finds that Oregon Revised Statutes § 57.175 does not apply to pre-existing voting trust agreements. The Court relies on Oregon Revised Statutes § 57.799 in support of its decision of inapplicability.

Oregon Revised Statutes, § 57.799 reads as follows:

“EFFECT OF REPEAL OF PRIOR ACTS. The repeal of a prior Act by chapter 549, Oregon Laws 1953, shall not affect any right accrued or established, or any liability or penalty incurred, under the provisions of such Act, prior to the repeal thereof. . .”

Oregon Revised Statutes § 57.799 quoted above applies only to a right accrued or established under laws repealed by the new Oregon Corporation Law. The old Oregon Corporation Law contained no provisions whatsoever relating to voting trusts, either condemning or condoning same. No prior statutory provision repealed by the new corporation law established any rights relating to voting trust agreements. Consequently, Oregon Revised Statutes § 57.799 is completely inapplicable.

Oregon Revised Statutes § 57.796(1) reads as follows:

“57.796. APPLICATION TO CORPORATIONS EXISTING ON DECEMBER 31, 1953. (1) The provisions of the Oregon Business Corporation Act shall apply to the fullest extent permitted by the laws and Constitution of the United States and of the State of Oregon,

to all existing corporations organized under any general Act of this state.”

Pilot Rock Lumber Co. was an existing corporation organized under a general act of the statute. Oregon Revised Statutes § 57.175 is a part of the *Oregon Business Corporation Act*. Consequently, Oregon Revised Statutes § 57.175 applies to the fullest extent permitted by the laws and Constitutions of the United States and of the State of Oregon. The nebulous status of voting trusts under Oregon law prior to Section 57.175 does not involve any constitutional issue, either state or federal. This leaves only Oregon law as a source for any provision which might preclude the applicability of Oregon Revised Statutes § 57.175 to a pre-existing voting trust agreement. As before mentioned, Oregon Revised Statutes Section 57.799 is inapplicable. No other statutory provision applies, and nothing in Oregon Revised Statutes § 57.175 itself makes any distinction between existing and future voting trust agreements. In contrast, some provisions of the new Oregon Business Corporation Law expressly provide that they shall not be applicable to existing agreements or documents. For example, Oregon Revised Statutes § 57.141 reads as follows:

“57.141. BYLAWS. The initial bylaws of a corporation shall be adopted by its board of directors. The power to alter, amend or repeal the bylaws or adopt new bylaws shall be vested in the board of directors unless reserved to the shareholders by the articles of incorporation or bylaws existing on December 31, 1953. . .”



Any applicability of *Western Pac. R. Corp. v. Baldwin*, cited by the Tax Court should be modified by the following quotation from the opinion (89 F.2d at 273):

“The Reconstruction Finance Corporation contends that, since Denver & Rio Grande is a Delaware corporation, and since the Delaware Corporation Law was amended in 1925—approximately one year after the voting trust agreement here involved was executed—so as to limit the maximum term of any voting trust agreement to ten years (34 Delaware Laws 1925, c. 112, § 6, p. 277), it must be held that no lawful extension of the voting trust agreement could be made. It is doubtful whether this issue of law was properly raised in the court below. The statute of Delaware is not mentioned in the pleadings, but the question is argued in the briefs and was called to the attention of the trial court. There is nothing in the amendatory act which specifically makes it applicable to voting trust agreements executed prior to its adoption. . . .”

A similar statement is contained in *Wolf v. Roosevelt*, the other case cited in the Tax Court opinion. The pertinent quotation from *Wolf v. Roosevelt* reads as follows (49 N.E.2d at 503):

“ . . . a statute restricting the power of individuals to create or define their rights and obligations should not be construed in manner which would affect existing agreements unless the Legislature so provided in express terms or by plain implication. The Legislature has not so provided in section 130-c of the Real Property Law. It seems plain that the condition, imposed by the Legislature to voting trust agreements,—that they shall not be valid unless ‘approved by the court,’ could not be applied to contracts made at a time when no such approval was required by law unless it was the intent of the Legislature to terminate all existing voting trust agreements. . . .”

Both of the above cases cited by the Tax Court hold that a statutory provision relating to voting trusts will be given retroactive application where such is provided by the express terms or by the plain implication of the statute. It is respectfully submitted that the implication of Oregon Revised Statutes § 57.175 itself favors retroactive application, and any doubt in this regard is eliminated by the express provision of Oregon Revised Statutes § 57.796 discussed above.

While the foregoing supports petitioner's position that Oregon Revised Statutes § 57.175 definitely invalidated the voting trust agreement, petitioner's position is not solely dependent thereon. It is sufficient if Oregon Revised Statutes § 57.175 cast a pall of invalidity upon the voting trust which pall could only be eliminated through judicial clarification or through mutual agreement of all the parties concerned, neither of which occurred during 1954, the only year in question. Such pall of invalidity is just as effective as positive invalidity under the practical approach hereinafter suggested by petitioner as the appropriate test to be applied in determining whether petitioner's own stock possessing 80% of the voting power.

Petitioner owned 74,000 out of 120,000 shares of outstanding common stock of Oregon Fibre Products, Inc. This is less than 80% of the outstanding shares. There is no issue concerning the preferred stock, it being stipulated that such stock does not possess voting rights and is limited and preferred as to dividends which, under the terms of § 1504, excludes it from the definition of "stock."



To qualify under the consolidated return requirements, it is necessary that there not be counted the 30,000 shares of stock held by the voting trustees under the voting trust agreement dated November 3, 1952. Petitioner's argument for not counting such 30,000 shares is based upon the difference between the phraseology of the applicable code provision here involved, and the phraseology of the corresponding code provision involved in all of the prior recorded cases having any pertinency to the issue. § 1504(a)(2), the pertinent provision of the Internal Revenue Code of 1954, here applicable, reads as follows:

“(2) The common parent corporation owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of at least one of the other includible corporations.”

The corresponding code provision involved in the prior cases reads as follows:

“The common parent corporation owns directly at least ——— percentum of each class of stock of at least one of the other includible corporations.”

Under the last-quoted provision, it would be necessary for petitioner to argue that the suspension of voting rights resulting under the voting trust converted the 30,000 shares into nonvoting stock so as to fall within the exclusion from the term “stock” of nonvoting stock which is limited and preferred as to dividends. Petitioner makes no such argument. It recognizes that the 30,000 shares were outstanding and that they do not fall within the beforementioned exclusion.

It does not necessarily follow that the 30,000 shares must be counted for consolidated return purposes just because the shares are outstanding and do not fall within the exclusion. The above-quoted phraseology of applicable § 1504(a)(2) requires only that the parent own *stock possessing at least 80% of the voting power*, which is substantially different from the requirement under a prior provision that the parent own at least the specified percent of each class of stock. It is possible to own stock possessing 80% of the voting power without owning 80% of the voting stock. This is clear from the differences in phraseology between § 1504(a)(2), and forms the very basis of petitioner's argument. To repeat,—it is possible to own stock possessing at least 80% of the voting power without owning 80% of the voting stock.

A case having a fact situation closest to that here involved is *Kansas O. & G. Ry. Co. v. Helvering*, 124 F.2d 460. A concise review and analysis of this case is contained in the following quotation from the opinion of this Court in *Pioneer Parachute Co.*, 6 T.C. 1246 at 1251-1252:

“We have not been furnished by either the petitioner or the respondent with any direct authorities on the solution of the question with which we are confronted, and it is not our intention to indulge in any prolonged discussion of the authorities cited. However, the powers of the class B preferred stockholders in this case do bear considerable analogy to those of the holders of the voting trust certificates involved in the case of *Kansas O. & G. Ry. Co. v. Helvering*, 124 Fed. (2d) 460. In that case, pending a reorganization, the stockholders and bondholders

of the petitioner railway delivered their stocks and bonds to a voting trustee to enable the trustee to act in the contemplated reorganization. After the voting trust was terminated notice was sent to all of the stockholders to reclaim their stock, but a substantial percentage neglected to do so. However, a consolidated return was filed by the affiliated group of corporations, including the reorganized railway, and the Commissioner questioned the right to a consolidated return because, if the voting shares of stock held by the trustee but unclaimed by the owners were counted, the parent company would not own the necessary percentage of the voting stock to permit a consolidated return. The court held that the outstanding unclaimed stock should be so counted and denied the privilege of filing a consolidated return. In so holding the court said:

“ ‘Nor is it of any consequence that the trust receipt holders cannot vote the stock to which they are entitled until stock certificates therefor have been issued to them. The stock is voting none the less. *It is the voting privilege with which a particular stock issued is endowed and not whether it is voted which determines its voting character within the intent of the Revenue Act of 1932 and 1934.*’ (Italics supplied)

“In that case the stockholder was required only to present his receipt and demand delivery of the voting stock from the voting trustee in order to acquire that stock. In the case at bar the holders of class B stock at any time had only to present their class B stock to the secretary of the company and demand their common voting stock in order to acquire the same.”

In *Kansas O. & G. Ry. Co. v. Helvering*, the taxpayer contended that suspension of voting rights by virtue of the unclaimed certificates in the terminated voting trust converted such unclaimed stock into nonvoting



stock qualifying under the statutory exclusion from the term "stock." This contention was necessary because the law then required ownership of a specified percentage of the stock,—not stock possessing a specified percentage of the voting power. What if the consolidated return requirements in *Kansas O. & G. Ry. Co. v. Helvering* was the same as in the present § 1504(a)(2)? Would not the parent have owned stock possessing the requisite percentage of the voting power? A negative answer might be based upon the fact that in *Kansas O. & G. Ry. Co. v. Helvering* the stockholder of the unclaimed certificate was required only to present his receipt and demand delivery of the voting stock from the voting trustee in which case the parent would not own stock possessing the requisite percentage of the voting power.

In the instant situation, the voting trust agreement dated November 3, 1952 containing the 30,000 shares was not terminated during 1954, and the voting trust certificate holders could not have received their voting shares from the trust by merely requesting same. Until the certificates were released from the voting trust and issued in the names of the certificate holders, the shares could not be voted by the certificate holders. Neither could the shares be voted by the voting trustees. A definite pall of invalidity was cast upon the voting trust by the Oregon Business Corporation Act adopted during the 1953 session of the Oregon legislature which became effective December 31, 1953. Section 32 of this Act (now Oregon Revised Statutes § 57.175) provides that a voting trust can be created for a period not to exceed ten

years. The voting trust agreement dated November 3, 1952 had a duration of 20 years. Such duration violated the ten year maximum specified in the before-mentioned statutory provision. Pending judicial clarification of the impact of this statutory provision upon a pre-existing voting trust, the voting trustees could not validly exercise their voting rights under the voting trust. Neither could the voting trust certificate holders exercise same until the stock was issued in their names. In the absence of a judicial determination, the matter could be resolved solely through a *mutual* termination of the voting trust agreement. No judicial determination was obtained or made during 1954, and the voting trust agreement was not terminated until January 1, 1955. Qualification to file consolidated returns after January 1, 1955 is no longer at issue.

From the December 31, 1953 effective date of the Oregon Business Corporation Act to the termination of the voting trust on January 1, 1955, the voting rights on the 30,000 shares in the voting trust were suspended by the impact of the ten year maximum voting trust duration specified in the new corporation law upon the pre-existing voting trust having a remaining duration substantially in excess of ten years. The 30,000 shares were voting stock, but the voting rights were definitely suspended during the full calendar year 1954.

With the voting rights suspended on the 30,000 shares, the 74,000 shares owned by petitioner possessed 80% of the voting power. Ownership of stock possessing 80% of the voting power is all that is required by



§ 1504(a)(2). It is not necessary that petitioner own 80% of the voting stock.

Petitioners submit that the practical approach should be adopted in determining whether there is stock ownership possessing 80% of the voting power. The practical approach can be applied through an assumed holding of a stockholders' meeting at any given moment during the subject year. At any such stockholders' meeting, how would the voting power of the stock owned by the parent compare with the total voting power which could be marshalled at any such meeting? All during 1954, petitioner owned 74,000 shares of the voting common stock. What voting power could have been marshalled against petitioner at any stockholders' meeting held at any time during 1954? Not, certainly, the 30,000 shares held by the voting trustees under a 20 year voting trust which applicable Oregon law authorizes for a period not in excess of 10 years. This leaves only the 16,000 shares owned by other individuals. Therefore, petitioner during 1954 owned stock possessing more than 80% of any voting power which could be marshalled at a stockholders' meeting held during 1954.

Petitioner's argument can be illustrated by analysis of the opinion in *Doernbecher Mfg. Co. v. Commissioner* (C.C.A. 9th, 1935), 80 F.2d 573, which affirmed a decision of this Court. In this case, the petitioner was the subsidiary corporation contending for consolidated return qualification. The petitioner was a party to a contract under which it was purchasing certain shares of its own stock. If these shares were not counted, there would have been the requisite stock ownership by the

parent. The pertinent portion of the Court's opinion reads as follows (80 F.2d at 574-575):

" . . . The petitioner relies upon a provision of its contracts to purchase the 9,152½ shares of stock, which is as follows: 'It is hereby expressly agreed that until the first party shall have foreclosed on said stock, as herein provided for, that said first party shall have no right to vote or draw dividends on said stock, or any part thereof, either in person or by proxy, it being expressly understood and agreed that the purchase price when paid is in full payment for said stock as of the date hereof.' Consequently, it is argued that this stock having been deprived of its voting and dividend privileges is expressly excluded from the stock to be considered in arriving at the 95 per cent. required by section 141 (d) of the Revenue Act of 1928 (26 U.S.C.A. Sec. 141 note) by that portion of the section which we quote: 'As used in this subsection the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.' Rev. Act 1928, Sec. 141(d)(2), 26 U.S.C.A. Sec. 141 note."

\* \* \* \* \*

" . . . The provision of the agreement for the sale of the stock above referred to with reference to the right of the seller to vote or draw dividends before foreclosure, whatever its effect, did not change the classification of the stock to 'non voting stock which is limited and preferred as to dividends.' Section 141 (d)(2), Rev. Act 1928, 26 U.S.C.A. Sec. 141 note, supra. It was still voting stock even if the right of the seller to vote it was temporarily suspended."

Petitioner in the instant proceedings agrees that the suspension of the voting rights on the 30,000 shares in the voting trust did not change the classification of the shares of nonvoting stock. The 30,000 shares were voting stock even though the voting rights thereon were

suspended during 1954. While such suspension of voting rights does not convert the 30,000 shares into nonvoting stock, such suspension does have a definite bearing upon the voting power possessed by the remaining shares. Any consideration of this point was not pertinent in *Doernbecher Mfg. Co.* because the qualification provision was different,—requiring ownership of the requisite percentage of the voting stock, not merely ownership of stock possessing the requisite voting power. A temporary suspension of voting power necessarily increases the voting power possessed by the remaining shares. The 30,000 shares did not possess effective voting power during 1954, so the 74,000 shares owned by petitioner possessed more than 80% of the voting power which could be marshalled at any stockholders' meeting held during 1954.

### CONCLUSION

Petitioner respectfully urges that the ultimate conclusion of the Tax Court is erroneous. Further, the subsidiary findings of the Tax Court are erroneous and do not support its ultimate finding. Petitioner, at all times during the year 1954 owned stock of Oregon Fibre Products, Inc., possessing 80% of the voting power of said corporation, and was, therefore, entitled to file a consolidated return with said corporation.

Respectfully submitted,

MAUTZ, SOUTHER, SPAULDING, KINSEY  
& WILLIAMSON,  
By WILLIAM H. KINSEY.

